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UNCLAS SECTION 01 OF 02 ASUNCION 000732

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SUBJECT: PARAGUAY - RAPID GROWTH OF MAQUILA SECTOR

REF: 05 ASUNCION 926

SUMMARY

¶1. Exports from Paraguayan maquilas (low-tax, export-oriented manufacturing or service businesses) are growing rapidly. From 2006 through 2007, the Paraguayan Ministry of Industry and Commerce (MIC) expects to receive over USD 40 million in additional foreign investment in the sector. Paraguay still faces some obstacles exporting to larger MERCOSUR members, but overall the GOP believes the investment and growth in maquilas will contribute greatly to national employment and economic growth. One of the ten components of Paraguay's MCC Threshold Program, which is just getting under way, involves support to the MIC for maquila sector development. End Summary.

LAW ALLOWS FOR MAQUILA PRESENCE IN PARAGUAY

¶2. In 2000, the GOP passed Maquila Law 1064/97 in an effort to attract new investment and create alternatives to employment in the informal sector. Paraguay's maquila regime allows maquila operations to be established anywhere in the country, provides for very low taxation of value-added, and provides for some limited domestic sales. The maquila regime applies both to manufacturing as well as services such as call centers or software development. Maquilas have been operating in Paraguay since 2001 and are achieving rapid growth not only from exports to MERCOSUR, but also to less traditional markets such as Thailand, China, Luxembourg, Korea, Japan, and Taiwan.

MAQUILA SECTOR EXPERIENCING UNPRECEDENTED GROWTH

¶3. Exports of products from the Paraguayan maquila sector are growing rapidly. As of May 2006, maquila exports reached USD 20.9 million, already 76% of total maquila exports in 2005. In May alone, exports were greater than USD 5.4 million, the largest monthly export level ever recorded and 70% higher than any previous monthly record. In the five-month period from January to May 2006 Paraguay had nearly three times the export value from maquilas as

during the same period in 2005, representing a 199% increase. Exports to MERCOSUR as of May reached more than USD 10 million. Leather products have been some of the most successful, generating over USD 5 million of revenue within MERCOSUR and USD 6.5 million overall. Garments and wood molding are also major maquila exports.

FOREIGN INVESTMENT FUELING MAQUILA GROWTH AND NEW JOBS

¶4. According to Roberto Elias of the Consejo Nacional de las Industrias Maquiladoras de Exportacion (CNIME), the MIC, based on contact with potential investors, conservatively estimates that Paraguay's maquila sector will receive USD 41 million in foreign investment over the next two years. France would be the largest investor as the MIC is currently negotiating with the French technology company Alcatel, which is considering an investment of between USD 20 and 50 million dollars in the communications sector (telephone assembly). While Elias stressed the tentative nature of the estimates, he said that negotiations with France are well underway. Companies from Brazil, Spain Chile, and Argentina are also expected to make investments related to textiles, call centers, metals, bottled water, and furniture. The MIC expects the increases in foreign investment to create at least 2,600 new jobs. The possible investments include both new projects and the expansion of existing maquila operations.

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U.S. MARINES USING PARAGUAYAN MAQUILA PRODUCTS
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¶5. The Paraguayan company Welsheng Paraguay SRL is one of the oldest Paraguayan maquilas and produces orthopedic products such as

ASUNCION 00000732 002 OF 002

ankle, wrist, and back braces, cervical collars, and elbow and knee supports. Manufacturing for the Seattle based company La Pointique International, Welsheng Paraguay has entered the U.S. market and is now providing orthopedic supplies to the United States Marine Corps. Welsheng Paraguay products are certified by the FDA.

MERCOSUR NTBs TOUCH MAQUILA SECTOR

¶6. Paraguay's private sector consistently complains that Brazil and Argentina throw up bureaucratic non-tariff trade barriers (NTBs) to Paraguayan exports of anything but basic raw materials. Ana Chuang, head of the export department for Welsheng Paraguay, told the Economic Section's commercial specialist that Welsheng frequently encounters NTBs when exporting to Brazil and Argentina. For example, authorities in both Brazil and Argentina often question the authenticity of the certificate of origin and require excessive documentation. They also reportedly claim that products are made or processed in Paraguay, and question why neoprene used in the braces is not imported from MERCOSUR countries. The excess scrutiny causes delays that create disincentives for importers. Ms. Chuang stated that doing business with countries like Chile was a delight, and it is often easier to work with countries outside MERCOSUR.

COMMENT

¶7. Despite some obstacles within MERCOSUR, the recent growth of Paraguay's maquila sector has been impressive. The MIC has made the sector a priority, and the recent growth suggests that the MCC Threshold Program component designed to support the maquila regime has the opportunity to be very successful. The outcome of Paraguay's efforts to cajole Brazil and Argentina into reducing non-tariff barriers to internal trade within Mercosur will be important for the sector's continued growth, although the increasing share of non-Mercosur destinations bodes well even if those efforts are slow to bear fruit.

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